

SMITH INTERNATIONAL INC

Form DEF 14A

April 11, 2008

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
SCHEDULE 14A**

Proxy Statement Pursuant to Section 14(a) of the Securities
Exchange Act of 1934

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to §240.14a-12

Smith International, Inc.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- No fee required.
- Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

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NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

May 13, 2008

To Our Stockholders:

The Annual Meeting of Stockholders (the Annual Meeting) of Smith International, Inc. (the Company) will be held on **Tuesday, May 13, 2008**, at 9:00 a.m. local time, at 700 King Street, Wilmington, Delaware, to consider and take action on the following:

1. Election of two directors: Loren K. Carroll and Dod A. Fraser, each for a term of three years;
2. Approval of the Smith International, Inc. Third Amended and Restated 1989 Long-Term Incentive Compensation Plan;
3. Approval of an Amendment to the Restated Certificate of Incorporation to increase the Number of Authorized Shares of Common Stock; and
4. Ratification of Deloitte & Touche LLP as independent registered public accounting firm for 2008.

Your Board of Directors recommends a vote FOR Proposals 1, 2, 3, and 4.

Important Notice Regarding the Availability of Proxy Materials for the Stockholder Meeting to Be Held on May 13, 2008: This proxy statement, along with the 2007 Annual Report to Stockholders, are available on the following website: www.edocumentview.com/sii.

The Board of Directors has fixed the close of business on March 14, 2008 as the record date for determining stockholders who are entitled to notice of and to vote at the meeting.

By Order of the Board of Directors

Richard E. Chandler, Jr.
Secretary

Houston, Texas
April 11, 2008

YOUR VOTE IS IMPORTANT.

Please vote your proxy promptly so that your shares will be represented, even if you plan to attend the Annual Meeting. You can vote by Internet, by telephone, or by using the proxy card that is enclosed. Please see your proxy card for specific instructions on how to vote. Brokers cannot vote for Proposal 2 without your instructions.

PROXY STATEMENT

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P. O. Box 60068
Houston, TX 77205-0068

PROXY STATEMENT

The Board of Directors of Smith International, Inc. is soliciting your proxy to vote your shares of the Company's common stock (Common Stock) at the 2008 Annual Meeting. We are distributing this Proxy Statement and the accompanying proxy card beginning on or about April 11, 2008. We solicit proxies to give all stockholders of record an opportunity to vote on matters that will be presented at the Annual Meeting. In this Proxy Statement, you will find information to assist you in voting your shares. **Your vote is very important.**

GENERAL INFORMATION ABOUT VOTING

Except as otherwise specifically noted in this Proxy Statement, we, our, us, and similar words as well as Smith and Company refer to Smith International, Inc.

Who may vote?

You are entitled to vote your shares of our Common Stock if you are a stockholder of record on March 14, 2008. At the close of business on March 14, 2008, a total of 200,816,561 shares of Common Stock were outstanding and entitled to vote. Each share of Common Stock has one vote. The enclosed proxy card shows the number of shares that you are entitled to vote.

How do I vote?

Stockholders of record may vote in person or by telephone, internet or mail. If you are voting by mail, please sign, date and mail the enclosed proxy card. If you are voting by telephone or internet, please follow the instructions on the enclosed proxy card.

Whether or not you plan to attend the meeting, we encourage you to vote by proxy as soon as possible.

If you hold your shares in more than one type of account or your shares are registered differently, you may receive more than one proxy card. We encourage you to vote each proxy card that you receive.

If you choose to attend the meeting in person, you will be asked to present valid picture identification and, if you hold your shares through a broker, you will be asked to present a copy of your brokerage statement showing your stock ownership as of March 14, 2008. For directions to the meeting, contact the Doubletree Hotel Downtown Wilmington, Delaware at 302-655-0400.

How will my shares be voted?

If you vote by proxy, the individuals named on the proxy card (your proxies) will vote your shares in the manner you indicate. You may specify on your proxy card whether your shares should be voted for all of the nominees for director or your vote may be withheld with respect to one or more of the nominees. You may also specify whether you approve, disapprove or abstain from the other proposals.

If you sign and return your proxy card without indicating your voting instructions, your shares will be voted FOR the election of all nominees for director and FOR Proposals 2, 3, and 4.

What if my shares are held by a broker?

If your Common Stock is held by a broker, bank or other nominee (in street name), your broker must vote those shares in accordance with your instructions. However, if you do not give voting instructions to your broker

within ten days of the meeting, your broker may vote your shares for you on any matter that the New York Stock Exchange determines to be routine. If the broker cannot vote on a particular matter because it is not routine, there is a broker non-vote on that matter. Broker non-votes do not count as votes for or against Proposals 2 and 4, but will count as votes against Proposal 3. An abstention counts as a vote against a proposal. Abstentions and broker non-votes have no effect on the outcome of the election of directors.

If you hold your shares in street name and you wish to vote in person at the Annual Meeting, you will need to obtain a proxy from the broker or nominee that holds your shares. If the meeting is adjourned, your Common Stock will be voted as specified on your proxy card on the new meeting date, unless you have revoked your proxy instructions.

May I revoke or change my vote?

You may revoke or change your proxy at any time before it is exercised by submitting written notice of revocation to Smith's Corporate Secretary so that he receives it before the Annual Meeting; voting again by telephone, internet or mail; or voting in person at the Annual Meeting.

Attendance at the Annual Meeting will not by itself revoke a previously granted proxy. If you hold your shares in street name and you wish to change your vote at the Annual Meeting, you will need to obtain a proxy from the broker or nominee that holds your shares.

What constitutes a quorum?

The holders of a majority of the outstanding shares of Common Stock entitled to vote constitutes a quorum for the transaction of business at the Annual Meeting. If you have returned valid proxy instructions or attend the meeting in person, your Common Stock will be counted for the purpose of determining whether there is a quorum, even if you wish to abstain from voting on some or all matters introduced at the meeting. Broker non-votes also count for quorum purposes.

How many votes are required to approve a proposal?

Directors (Proposal 1) must be elected by a plurality of the votes cast at the meeting. This means that the two nominees receiving the greatest number of votes will be elected. The affirmative vote of a majority of the shares represented at the meeting and entitled to vote on a particular matter is required to approve Proposals 2 and 4. The affirmative vote of a majority of the outstanding shares is required to approve Proposal 3. Broker non-votes do not count as votes for or against Proposals 2 and 4, but will count as votes against Proposal 3. An abstention counts as a vote against a proposal. Abstentions and broker non-votes have no effect on the outcome of the election of directors.

What other matters will be acted upon at the meeting?

We do not know of any other matters that will be presented at the Annual Meeting, other than those mentioned in this Proxy Statement.

Who pays the cost of this proxy solicitation?

We will pay the cost of solicitation of proxies including preparing, printing and mailing this Proxy Statement. We have retained Morrow & Co. to help us in soliciting proxies for a fee of \$7,500, plus reasonable out-of-pocket costs and expenses. We will also reimburse brokers, banks and other nominees for their costs in sending proxy materials to beneficial owners of our Common Stock. Other proxy solicitation expenses that we will pay include those for preparation, mailing, returning and tabulating the proxies.

PROPOSAL 1: ELECTION OF DIRECTORS

At the Annual Meeting, stockholders will elect two persons as Class I directors to hold office until the 2011 Annual Meeting, or until they are succeeded by other qualified directors who have been appointed or elected. The nominees are Loren K. Carroll and Dod A. Fraser.

Directors must be elected by a plurality of the votes cast at the meeting. This means that the two nominees receiving the greatest number of votes will be elected. Votes withheld for any director will not be counted. We will vote your shares as you specify on your proxy card. If you properly execute and return your proxy card (in paper form, electronically via the internet or by telephone), but do not specify how you want your shares voted, we will vote them *for the election of all of the nominees listed below.*

Each of the nominees is a current member of the Board of Directors and has consented to serve if elected. Although management does not contemplate the possibility, in the event any nominee is not a candidate or is unable to serve as a director at the time of the election, the proxies will vote for any nominee who is designated by the present Board of Directors to fill the vacancy.

A brief biography of all directors is presented below:

NOMINEES

Directors to be elected to Class I for a term expiring in 2011:

LOREN K. CARROLL

Age:	64
Director Since:	1987
Recent Business Experience:	Mr. Carroll joined the Company in December 1984 as Vice President and Chief Financial Officer. He is currently an advisor to the Company. From March 1994 until April 2006, Mr. Carroll served as President and Chief Executive Officer of M-I SWACO, a company in which the Company holds a 60% interest. From 1992 until 1994, he served as Executive Vice President and Chief Financial Officer of the Company. In January 1988, he was appointed Executive Vice President and Chief Financial Officer and served in that capacity until March 1989. He rejoined the Company in 1992.
Committee Membership:	None
Other Directorships:	Fleetwood Enterprises, Inc.; CGG-Veritas; Forest Oil Corporation; KBR, Inc.

DOD A. FRASER

Age:	57
Director Since:	2004
Recent Business Experience:	Mr. Fraser is the President of Sackett Partners Incorporated, a consulting company, and a member of corporate boards. Mr. Fraser established Sackett

Partners in 2000 upon retiring from a 27-year career in investment banking. From 1995 to 2000, Mr. Fraser was with The Chase Manhattan Bank, now JP Morgan Chase, where he was Managing Director, Group Executive of the global oil and gas group. Prior to that, Mr. Fraser was General Partner of Lazard Freres & Co., which he joined in 1978.

Committee Membership:

Chairman, Audit Committee; Compensation and Benefits Committee.

Other Directorships:

Forest Oil Corporation; Terra Industries, Inc.

WE RECOMMEND A VOTE FOR THE ELECTION OF THE DIRECTOR NOMINEES.

DIRECTORS CONTINUING IN OFFICE

Class II directors to continue in office until 2009:

ROBERT KELLEY

Age: 62

Director Since: 2005

Recent Business Experience: Since 2001, Mr. Kelley has served as the President of Kellco Investments, a private investment company. From 1986 to 2001, Mr. Kelley served in several senior management roles including Chairman, President and Chief Executive Officer of Noble Affiliates, Inc. Prior to 1986, he was President and Chief Executive Officer of Samedan Oil Corporation, a subsidiary of Noble Energy Inc.

Committee Membership: Audit Committee; Compensation and Benefits Committee.

Other Directorships: Cabot Oil and Gas Corporation; OGE Energy Corp.

DOUG ROCK

Age: 61

Director Since: 1987

Recent Business Experience: Mr. Rock was elected Chairman of the Board of Directors on February 26, 1991. Mr. Rock has been with the Company since 1974 and has been Chief Executive Officer, President and Chief Operating Officer since March 31, 1989.

Committee Membership: None

Other Directorships: Moneygram International, Inc.

Class III directors to continue in office until 2010:

JAMES R. GIBBS

Age: 63

Director Since: 1990

Recent Business Experience: Mr. Gibbs is the Chairman of the Board, President & Chief Executive Officer of Frontier Oil Corporation. He was President and Chief Operating Officer of Frontier from January 1, 1987 to April 1, 1992, at which time he assumed the additional position of Chief Executive Officer. He was elected Chairman of the Board of Frontier in April 1999. He joined Frontier Oil Corporation in February 1982 as Vice President of Finance and Administration, and was appointed Executive Vice President in September 1985.

Committee Membership: Chairman, Nominating and Corporate Governance Committee.

Other Directorships: Frontier Oil Corporation; advisory director of Frost Bank-Houston; member of the Board of Trustees of Southern Methodist University.

JOHN YEARWOOD

Age: 48

Director Since: 2006

Recent Business Experience: Mr. Yearwood, a citizen of Trinidad and Tobago, has served as a Senior Advisor to the Chief Executive Officer of Schlumberger since March 2006. From 1980 to March 2006, he served in a variety of positions at Schlumberger Limited much of which included responsibilities for businesses primarily focused outside of the United States, most recently as President North and South America, Oilfield Services.

Committee Membership: Audit Committee; Nominating and Corporate Governance Committee.

Other Directorships: Logan Oil Tools; Sheridan Production Partners; Remora Energy; NFR Energy.

DIRECTORS NOT CONTINUING IN OFFICE:**G. CLYDE BUCK**

Age: 70

Director Since: 1992

Recent Business Experience: Mr. Buck has extensive experience in energy-related matters. He received a B.A. in economics from Williams College and a M.B.A. from Harvard. He is currently affiliated with Davis/Chambers & Company, Ltd., a position he has held since January 1, 2008. From April 1998 until December 2007, he was a Senior Vice President and Managing Director of Corporate Finance of the investment banking firm of Sanders Morris Harris Inc. From 1983 to 1998, Mr. Buck was a Managing Director in the Houston corporate finance office of Dain Rauscher Incorporated.

Committee Membership: Chairman, Compensation and Benefits Committee; Nominating and Corporate Governance Committee

Other Directorships: Frontier Oil Corporation.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table shows certain information about stock ownership of all persons known to the Company to own of record or beneficially more than 5% of the outstanding Common Stock of the Company. This information is based upon information furnished to the Company by these persons and statements filed with the SEC:

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class
T. Rowe Price Associates, Inc. 100 East Pratt Street Baltimore, Maryland 21202	20,173,160(1)	10.05%
FMR LLC 82 Devonshire Street Boston, Massachusetts 02109	18,978,796(2)	9.45%

- (1) Based upon the statement on Schedule 13G filed with the Securities and Exchange Commission on February 13, 2008. These securities are owned by various individual and institutional investors for which T. Rowe Price Associates, Inc. (Price Associates) serves as investment adviser with power to direct investments and/or sole

power to vote the securities. For purposes of the reporting requirements of the Securities Exchange Act of 1934, Price Associates is deemed to be a beneficial owner of such securities; however, Price Associates expressly disclaims that it is, in fact, the beneficial owner of such securities.

- (2) Based upon the statement on Schedule 13G filed with the Securities and Exchange Commission on February 14, 2008. Such filing indicates that FMR LLC has sole voting power over 815,374 shares and sole dispositive power over 18,978,796 shares of Common Stock.

The following table shows the number of shares of Common Stock beneficially owned as of March 15, 2008 by each director or nominee for director, the executive officers named in the Summary Compensation Table included later in this Proxy Statement and all directors and executive officers as a group. Except as otherwise indicated, the persons listed below have sole voting power and investment power relating to the shares shown.

Name of Beneficial Owner	Amount and Nature of Beneficial Ownership(1)(2)	Percent of Class
G. Clyde Buck(3)	68,136	*
Loren K. Carroll	183,411	*
Margaret K. Dorman(4)	167,501	*
Bryan L. Dudman(4)	34,246	*
Dod A. Fraser	11,508	*
James R. Gibbs(3)(5)	30,536	*
Robert Kelley	11,994	*
John Kennedy	59,597	*
Donald McKenzie	38,743	*
Doug Rock	724,433	*
John Yearwood	4,785	*
All directors and executive officers as a group (15 persons)(4)	1,379,539	*

* Less than 1%

- (1) The amounts reported do not include the shares of Common Stock to be issued to each outside director on or about April 25, 2008 under the Smith International, Inc. Second Amended and Restated 1989 Long-Term Incentive Compensation Plan. The shares to be issued will be based on the closing price of the Company's Common Stock on the date of such issuance and will be a number of shares to give each outside director equity compensation of approximately \$200,000.
- (2) The amounts reported include shares of Common Stock that could be acquired within 60 days of March 15, 2008 through the exercise of stock options as follows: Mr. Rock: 169,500 shares; Mr. Carroll: 59,000 shares; Ms. Dorman: 128,000 shares; Mr. Dudman: 2,400 shares; Mr. Kennedy: 26,500 shares; and all directors and executive officers as a group: 386,300 shares.
- (3) The amounts reported do not include 24,000 restricted stock units held by Messrs. Gibbs and Buck. Each such restricted stock unit represents a contingent right to receive one share of Common Stock and were granted to each of Messrs. Buck and Gibbs in 1999 in connection with the termination of the Directors' Retirement Plan, which will not be issued until the restricted stock units vest upon retirement after ten years of service as a director. Messrs. Buck and Gibbs currently have no voting or investment power with respect to the related shares of Common Stock. Although Mr. Buck retires from his service as a director as of the Annual Meeting, he has deferred receipt of his shares for three years.
- (4) The amounts reported include shares of Common Stock allocated to accounts under a 401(k) plan as follows: Ms. Dorman: 5,344 shares; Mr. Dudman: 23,993 shares; and all directors and executive officers as a group:

29,449 shares. This amount does not include 1,100,056 shares beneficially held by Jerry W. Neely who currently serves as an Advisory Director to the Board.

(5) The amounts reported include 2,000 shares held by Mrs. Gibbs.

CORPORATE GOVERNANCE

Corporate Governance Guidelines

Our Corporate Governance Guidelines outline the functions of the Board, director qualifications and responsibilities, and various processes and procedures designed to ensure effective and responsive governance. The full text of the guidelines is published on our website at www.smith.com under the Investor Relations caption and link to Governance. Stockholders may also obtain a free copy upon request by contacting the Corporate Secretary, Smith International, Inc., 16740 East Hardy Road, Houston, Texas 77032.

Board Structure

Our Board of Directors currently consists of seven directors. Board agendas include regularly scheduled sessions for the independent directors to meet without management present. The Board has designated Mr. Gibbs as Lead Director to chair executive sessions of the non-management directors.

G. Clyde Buck has reached retirement age pursuant to our Corporate Governance Guidelines and is, therefore, not standing for re-election as a director. Upon completion of Mr. Buck's service as a director on May 13, 2008, the Board will reduce its size to six members. At that time, it is anticipated that Mr. Buck will become an advisory director to the Board. In this capacity, Mr. Buck will be invited to attend meetings of the Board and its committees and will have access to materials distributed to the Board, but will not be entitled to vote at such meetings.

Board Meetings

The Board and its committees meet throughout the year on a set schedule, and also hold special meetings and act by written consent from time to time as appropriate. The Board of Directors held five meetings during 2007. All directors attended at least 75% of the meetings of the Board of Directors and of all committees on which they served. The Company does not have a policy regarding directors' attendance at the Annual Meeting of Stockholders. No directors attended the 2007 Annual Meeting.

Director Independence

The Board annually evaluates the independence of the directors and has affirmatively determined that all directors (including Jerry W. Neely who served as a director during the 2007 year until April 25, 2007) are independent except Doug Rock and Loren Carroll, who are employees of the Company. The Board's determination regarding independence and financial expertise of its members is based on applicable laws and regulations, Smith's Corporate Governance Guidelines, the rules of the New York Stock Exchange and a review of any direct or indirect relationship between each director or his immediate family and Smith. To be considered independent, the Board of Directors must affirmatively determine that a director has no material relationship with Smith. In each case, the Board of Directors broadly considers all relevant facts and circumstances, including the director's commercial, industrial, consulting, legal, accounting, charitable and familial relationships and such other criteria as the Board of Directors may determine from time to time. In evaluating the independence of each non-employee director, the Board considered that in the ordinary course of business our subsidiaries buy from or sell to companies with which our directors have relationships as follows:

(1) Mr. Gibbs is Chairman of the Board, President & Chief Executive Officer of, and Mr. Buck is a director of, Frontier Oil Corporation.

(2) Mr. Fraser is a director of Forest Oil Corporation.

(3) Mr. Kelley is a director of Cabot Oil and Gas Corporation and OGE Energy Corp.

(4) Mr. Yearwood is a director of Logan Oil Tools and Sheridan Production Partners and is a senior advisor to Schlumberger. Schlumberger is also the minority partner in our M-I SWACO business unit, a 60 percent-owned joint venture.

With respect to each of the most recent three completed fiscal years, none of the payments to or payments received from any of the companies for which our directors are employees exceeded the greater of \$1.0 million or

2% of such company's consolidated gross revenues. All of these companies expect to continue their business relationship in 2008.

Communication with the Board

Stockholders and interested parties who wish to communicate with the non-management directors as a group, the Lead Director, or with any individual director, may do so by contacting Smith's Corporate Secretary at 16740 East Hardy Road, Houston, Texas 77032. Smith's Corporate Secretary will then relay all communications to the appropriate director or group of directors.

Committees of the Board

The Board has delegated various responsibilities and authority to different Board Committees as described in this section of this Proxy Statement. The Board has determined that all committee members are independent and satisfy the relevant additional independence requirements for the members of such committees imposed by the SEC or the Company. Each committee operates under a formal charter adopted by the Board, the full text of which may be found on our website at www.smith.com under the Investor Relations caption and link to Governance. Stockholders may also obtain a free copy upon request by contacting the Corporate Secretary, Smith International, Inc., 16740 East Hardy Road, Houston, Texas 77032.

Members of the Committees of the Board.

	Audit Committee		Compensation and Benefits Committee		Nominating and Corporate Governance Committee	
G. Clyde Buck			X	*	X	
Loren K. Carroll						
Dod A. Fraser	X	*	X			
James R. Gibbs					X	*
Robert Kelley	X		X			
Doug Rock						
John Yearwood	X				X	

* Committee Chairman

Audit Committee. During 2007, the Audit Committee met ten times, including telephone meetings, to discuss relevant accounting, auditing, internal control and disclosure matters. The Audit Committee's responsibilities, discussed in detail in the charter include, among other duties, the responsibility to:

- assist the Board in its general oversight of Smith's auditing, financial reporting and internal control functions;
- appoint, compensate and oversee the work of Smith's independent registered public accounting firm;
- review the Company's compliance with corporate governance standards; and

review the work and performance of the Company's internal audit function.

The Board of Directors has determined that all members are financially literate and that all members qualify as audit committee financial experts.

Compensation and Benefits Committee. During 2007, the Compensation and Benefits Committee met seven times. The Compensation and Benefits Committee charter permits the Compensation and Benefits

Committee to delegate its authority to sub-committees. The Compensation and Benefits Committee's responsibilities, discussed in detail in the charter include, among other duties, the responsibility to:

review the Company's executive compensation program, including approving corporate goals and objectives relating to CEO compensation and evaluating CEO performance in light of such goals and objectives;

review the Company's employee benefits and incentive compensation plans and programs, including their establishment, modification and administration;

review and make recommendations to the Board with respect to director compensation; and

review and discuss the compensation discussion and analysis with management and recommend its inclusion in this Proxy Statement.

Nominating and Corporate Governance Committee. During 2007, the Nominating and Corporate Governance Committee met five times. The Nominating and Corporate Governance Committee's responsibilities, discussed in detail in the charter include, among other duties, the responsibility to:

monitor developments in corporate governance principles and standards and develop and recommend to the Board a set of corporate governance guidelines;

identify and review the qualifications of director candidates and make recommendations for Board membership and structure;

review and evaluate the effectiveness of the Company's management succession plan; and

administer a process to measure the effectiveness of the Board and its committees.

Director Qualifications and Nominations

The Nominating and Corporate Governance Committee will consider nominees proposed by stockholders. To recommend a prospective nominee for the Nominating and Corporate Governance Committee's consideration, you may submit the candidate's name and qualifications to Smith's Corporate Secretary at 16740 East Hardy Road, Houston, Texas 77032. Recommendations from stockholders for nominees must be received by Smith's Corporate Secretary not later than the date set forth under the section "Stockholders' Proposals."

The process for identifying and evaluating director nominees includes the following steps:

(1) the Nominating and Corporate Governance Committee, Chairman of the Board or other Board members identify a need to fill vacancies or add newly created directorships;

(2) the Chairman of the Nominating and Corporate Governance Committee initiates a search and seeks input from Board members and senior management and, if necessary, hires a search firm or obtains advice from legal or other advisors;

(3) director candidates, including any candidates properly proposed by stockholders in accordance with the Company's Bylaws, are identified and presented to the Nominating and Corporate Governance Committee;

(4) initial interviews of candidates are conducted by the Chairman of the Nominating and Corporate Governance Committee;

(5) the Nominating and Corporate Governance Committee meets to consider and approve final candidate(s) and conduct further interviews as necessary; and

(6) the Nominating and Corporate Governance Committee makes recommendations to the full Board for inclusion in the slate of directors at the Annual Meeting.

The evaluation process will be the same whether the nominee is recommended by a stockholder or by a member of the Board of Directors. The Nominating and Corporate Governance Committee is responsible for establishing the selection criteria for candidates from time to time and reviewing with the Board such criteria and the appropriate skills and characteristics required of Board members in the context of the then current make-up of the Board. At a minimum, the Nominating and Corporate Governance Committee must be satisfied that each

nominee for director has the necessary business and/or professional knowledge and experience relevant to the Company, its business and the goals and perspectives of its stockholders; is well regarded in the community, with a long term, good reputation for high ethical standards; has good common sense and judgment; has a positive record of accomplishment in present and prior positions; has an excellent reputation for preparation, attendance, participation, interest and initiative on other boards on which he or she may serve; and has the time, energy, interest and willingness to become involved in the Company and its future.

Compensation Committee Interlocks and Insider Participation

During 2007, Messrs. Gibbs (until April 25, 2007), Buck, Fraser and Kelley served as members of the Company's Compensation and Benefits Committee. None of the Compensation and Benefits Committee members has served as an employee or officer of the Company, and none of the Company's executive officers has served as a director or member of the compensation committee of another entity, which has an executive officer serving as a member of the Company's Board.

Code of Business Conduct and Ethics

All of our officers, employees and directors are required to comply with our Code of Business Conduct and Ethics to help ensure that our business is conducted in accordance with the highest standards of ethical behavior. Our Code of Business Conduct and Ethics covers all areas of professional conduct, including customer relationships, conflicts of interest, insider trading, financial disclosure, intellectual property and confidential information, as well as requiring strict adherence to all laws and regulations applicable to our business. Employees may report any violations or suspected violations of the Code by using Smith's ethics hotline. The Code includes an anti-retaliation statement. The full text of the Code of Business Conduct and Ethics, as well as any waiver of a provision of the Code granted to any senior officer or director or material amendment to the Code, if any, is published on our website at www.smith.com under the Investor Relations caption and link to Governance. Stockholders may also obtain a free copy upon request by contacting the Corporate Secretary, Smith International, Inc., 16740 East Hardy Road, Houston, Texas 77032.

COMPENSATION DISCUSSION AND ANALYSIS

Overview

Compensation Objectives. We have designed our executive compensation program to reward our executives based on Company, business unit and individual performance. The general objectives of our executive compensation program are to:

attract and retain the best available individuals to serve on our executive team;

motivate our executives to achieve our short- and long-term financial and operational goals; and

align our executives' interests with those of our other stockholders.

Pay for Performance. We believe that executives should be rewarded for outstanding performance. Our compensation philosophy ties direct financial incentives in the form of cash awards and long-term equity awards to our annual performance goals. We base these performance goals on consolidated or business unit financial results, depending upon the executive officer's position with the Company. We reward individual performance through adjustments in annual base salary.

Decision Process. Our Compensation and Benefits Committee (referred to in this section as the Compensation Committee) makes all executive compensation decisions. The Compensation Committee has retained Frederic W. Cook & Co., Inc. (referred to in this section as Cook), an independent compensation consultant reporting solely to the Compensation Committee, to assist it in making executive compensation decisions.

In October of each year, Cook provides current and comparative compensation data, including benchmarking results as discussed below, to the Compensation Committee and makes preliminary compensation recommendations. For all executive officers other than the CEO, the Compensation Committee discusses Cook s

recommendations with our CEO and Senior Vice President of Human Resources and receives additional recommendations related to items such as individual and business unit performance and the Company's overall compensation objectives. With respect to CEO compensation, Cook recommends a level of equity compensation consistent with benchmarking results, but does not provide recommendations for base salary or annual cash bonus awards. Company management has no input into CEO compensation.

The Compensation Committee makes final compensation decisions in December each year to correspond with the Board of Directors' approval of the Company's upcoming fiscal year's business plan and with the Compensation Committee's evaluation of executive performance for the current year. The Compensation Committee meets separately in executive session to review the CEO's performance, set his performance objectives for the next fiscal year and set his compensation. Executive compensation decisions become effective January 1 of the upcoming fiscal year. With the exception of equity incentive awards for new hires or promotions, which are granted at the next regularly scheduled Compensation Committee meeting after the hire or promotion date, equity incentive awards are granted only in December.

Benchmarking Group. The worldwide energy industry is a competitive environment for executive talent. To attract and retain a high level of executive expertise, we must remain competitive with the pay of companies with whom we compete for executive talent. Cook provides us with general compensation information related to our industry and specific compensation information related to a group of companies in our industry whose executives have similar duties and responsibilities. The Compensation Committee generally attempts to provide total target compensation between the median and 75th percentile of the range of executive compensation paid by the benchmarking group, with variation based on levels of responsibility and contributions to the Company. The following companies compose our benchmarking group:

Baker Hughes Incorporated	Halliburton Company
BJ Services Company	National Oilwell Varco, Inc. (NOV)
Cameron International Corporation	Schlumberger Ltd.
FMC Technologies, Inc.	Weatherford International Ltd.
Grant Prideco, Inc. (prior to merger with NOV)	

Fixed v. Variable Pay. Our compensation program is divided into two general categories, fixed and variable pay. Fixed pay consists of base salary and provides the named executive officers with a level of assured cash compensation appropriate for their positions within the Company. Variable pay includes annual cash bonus awards and annual performance-based equity awards, each as explained in more detail below. The Compensation Committee believes that a substantial portion of total compensation should be at-risk to the named executive officers and tied to the Company's financial performance goals. Therefore, variable pay represents about 80% of a named executive officer's total target compensation and is not earned unless financial performance goals are met.

At the beginning of each year, the Compensation Committee approves consolidated and business unit performance matrices which set forth targets for the variable pay component of executive compensation. These matrices are based on the financial performance goals established in the Company's annual business plan. Because the goals are established in December of each year and market conditions fluctuate throughout the year, the performance goals may not correspond to subsequent annual earnings estimates released by the Company. We expect that each member of our senior management team will produce outstanding results and have established performance targets that are generally achievable under the annual business plan.

Executive Position Grade Levels. The Compensation Committee sets grade levels for each executive management position based on levels of responsibility and authority within the Company. The grade level for each individual

executive officer typically corresponds to his or her management position. To recognize the exceptional contributions of an individual executive officer, he or she may be placed in a grade level higher than the corresponding grade level for his or her management position. Variable pay awards and equity grants, as well as perquisite benefits, are consistent within each grade level.

Alignment of Interests with Stockholders. Equity-based compensation constitutes approximately 65% of our total target executive officer compensation. Performance measures are tied in large part to overall stockholder

wealth. Our emphasis on equity- and performance-based compensation provides our executives with incentive to create long-term stockholder value while keeping fixed base salary costs as one of the smallest components of total target compensation. Further, it is consistent with our compensation philosophy that our executive management should be rewarded when financial performance goals are met or exceeded, thereby creating value for our stockholders.

Executive Compensation Components

Below is a summary of the various components of executive compensation.

Annual Base Salary. The Compensation Committee does not use a specific formula for evaluating individual performance. Instead, executives are assessed primarily by the CEO based upon their contributions to the Company's business success. The CEO is assessed solely by the Compensation Committee in executive session. The criteria used in evaluating individual performance, including that of the CEO, vary depending on the executive's function, but generally include:

leadership inside and outside the Company;

advancing the Company's interests with customers, vendors and in other business relationships;

product quality and development;

advancement in skills and responsibility; and

financial results.

The Compensation Committee sets each executive's base salary in light of individual performance and the salary range paid by the benchmarking group. Representing about 20% of total target compensation, base salaries generally remain at the median level of the salary range but may increase to or exceed the 75th percentile for outstanding performance. Based on his leadership, business results, Company growth and future strategy development, Mr. Rock received a merit increase to base salary of 11%, effective January 1, 2008. In addition, the Compensation Committee increased the grade level of the management position held by Ms. Dorman, increasing her salary range and making her eligible for a higher percentage annual cash bonus target and a higher level of equity awards. As a result of these changes and in recognition of her individual performance, Ms. Dorman received a 15% salary increase, which places her at the median level. The Compensation Committee also increased Mr. Dudman's grade level, increasing his salary within the benchmarking group and making him eligible for a higher percentage annual cash bonus target and a higher level of equity awards. Mr. Dudman received a 21% salary increase which places him above the 75th percentile for the grade level of his management position, but provides target compensation equal to that of the President of M-I SWACO. In providing this change in grade level, the Compensation Committee recognized Mr. Dudman's excellent management skills, accomplishments in growing Smith Services to record performance levels and his leadership role within and future value to the Smith organization. All other named executive officers received merit increases in a range of 5% to 6%.

Annual Cash Bonus. Our executive officers participate in the Executive Officer Annual Incentive Plan (AIP) which provides for annual cash bonuses. The Compensation Committee ties approximately 18% of each named executive officer's total target compensation to the achievement of financial performance goals under the AIP.

Participants in the AIP can earn an annual cash bonus based upon the achievement of established financial performance goals for each fiscal year. The target annual bonus percentages for the executive officers are determined based upon the grade level of the executive officer and are generally close to the median of the benchmarking group. The payout award, if any, is determined by multiplying the actual annual bonus percentage earned by the executive's base salary in effect as of the beginning of the AIP's fiscal year. For the 2007 and 2008 performance years, the target annual bonus percentages and grade levels for the named executive officers are as follows:

Name	Performance Year			
	2007	2008	2007	2008
	Grade Level	Target AIP %	Grade Level	Target AIP %
D. Rock	I	120%	I	120%
M. Dorman	III	70%	II	80%
D. McKenzie	II	80%	II	80%
B. Dudman	III	65%	II	80%
J. Kennedy	III	65%	III	65%

The actual payout under the AIP for any fiscal year is variable and tied to consolidated performance for corporate officers or business unit performance for business unit officers. The financial performance goals are measured using two metrics, generally (i) earnings per share and (ii) return on equity; however, for business unit management, the metrics are defined as operating earnings and return on operating assets for that business unit. When consolidated, the business unit operating income goals and return on operating assets goals are aligned with the consolidated corporate earnings per share and return on equity goals. The Compensation Committee has chosen return on stockholder equity and earnings per share (and the related operating income and return on operating assets for the business units) as the performance measures for the AIP because these metrics are tied to overall stockholder wealth, are readily understood by the executives and provide a balanced incentive to increase income while managing the Company's investment in its net assets.

Depending upon performance, the payout can range from zero to 200% of the target annual cash bonus percentage. Upon the achievement of the target financial performance goals, participants earn 100% of their target annual cash bonus. Generally, the actual financial performance achieved must be 80% or more of both target metric goals in order to earn any payout under the AIP and must be 120% or more of both target metric goals in order to earn a payout under the AIP of 200% of the target amount. For the 2007 fiscal year, the corporate earnings per share goal was \$2.97 and the return on stockholder equity target was 27.2%. For the fiscal year ended December 31, 2007, the actual performance levels achieved by the Company and business units ranged from above to below the target goals, resulting in each named executive officer earning between 35% and 162% of their target annual cash bonus percentage.

The Compensation Committee has no discretion to increase any award once the performance targets have been established, but may decrease or eliminate any annual bonus award due to unacceptable individual performance, even if the financial performance targets are met. The AIP is intended to comply with Section 162(m) of the Internal Revenue Code of 1986 and, as such, amounts paid under the AIP are fully deductible by the Company for federal income tax purposes.

Annual Performance-Based Restricted Stock Unit Award. The annual performance-based restricted stock unit (Unit) award is the largest potential component of total target annual compensation. The Compensation Committee awards Units to the executive officers in December of each year under the Smith International, Inc. Second Amended and

Restated 1989 Long-Term Incentive Compensation Plan (LTICP). Units represent the right to receive shares of common stock in the future, depending upon the achievement of the consolidated return on equity goal for the coming year.

The Compensation Committee sets the monetary value of the awards by grade level, generally at the 60th to 65th percentile level for equity awards granted by the benchmarking group. Shares subject to Unit awards are not owned until the financial performance goal is obtained and the awards have vested, accordingly participants have no voting rights on the shares and do not receive dividends until the shares are earned and vested. The number of target

Units granted is determined based on the closing price of the common stock on the date of grant, discounted for the present value of the dividends that are not paid on the unvested shares. If the Units are earned at year end, they vest in equal installments over a three-year period, based on continued employment requirements.

Depending upon performance, the payout for the 2007 performance period could range from zero to 115% of the target number of Units awarded to the executive officers. Upon the achievement of the return on equity goal, participants earn 100% of the Units awarded. Generally, the actual financial performance achieved must be 80% or more of the return on equity goal in order to earn any Units and must be 110% or more of the return on equity goal in order to earn 115% of the target Unit award. After financial performance goals have been set, the Compensation Committee does not exercise any discretion in the amount of Units awarded. For the 2008 performance period, the payout range was changed to zero to 130%, with more aggressive financial performance required to achieve the maximum payout. For the 2007 fiscal year, the return on equity goal was 27.2%. For fiscal year ended December 31, 2007, the actual performance level achieved by the Company was above the maximum target goal, resulting in each individual earning 106.5% of their target Unit award.

In 2005, the Company made the decision to award Units rather than Non-Qualified Stock Options, which had been issued under the LTICP since 1989. In reaching the decision to award Units, the Compensation Committee evaluated, among other considerations, changes to the required accounting treatment of stock option awards and other tax and accounting implications of various types of equity awards. Awarding Units instead of Non-Qualified Stock Options reduces stockholder dilution because the Company can offer equal long term value while issuing fewer shares. Unit awards are earned only when the performance goal is met, contain a retention element and align executive management with stockholder interests. For these reasons, the Compensation Committee has determined that Units are the most appropriate long-term equity based incentive for our Company and are the only type of equity incentive that the Company currently awards to its executive officers.

Perquisites. The Company has an interest in ensuring the physical and mental wellness of its employees and, therefore, provides for a reimbursement of up to \$3,000 for an annual physical for each executive officer. In addition, in lieu of providing specific perquisites, the Company provides a set cash dollar amount of specifically identified perquisites. This dollar amount is consistent within each grade level and is paid in 26 equal bi-weekly payments annually, as identified in the footnotes to the Summary Compensation Table. The executive officers do not need to spend their allowance on the specified items, but are free to use the allowance at their discretion. We believe that providing a set dollar amount allows our executive officers more flexibility and is more efficient to administer than reimbursing for each individual expense. The amount provided is reviewed periodically and is consistent with perquisites provided by the benchmarking group. In addition, our executive officers may receive personal administrative assistant services at no incremental cost to the Company. Perquisite amounts are not considered annual salary for bonus purposes or 401(k) contributions.

401(k) Plan. The Company believes that financial security during retirement is an important benefit to provide to our executive management. For this reason, the Company and various subsidiaries offer 401(k) plans to their employees, including their executive officers. Because the Company and subsidiary plans operate and are administered in a similar fashion, for purposes of this discussion, the 401(k) plans will be referred to in the singular. Participants may contribute up to the federal limit in the 401(k) plan. The Company makes various levels of contributions to the 401(k) plan, including age-weighted contributions and performance-based matching contributions as defined in the 401(k) plan. Although the majority of the Company's peers have both defined benefit and defined contribution plans, the Compensation Committee elected to implement a defined contribution plan (the 401(k) plan) to control Company costs. The Company's 401(k) plan is consistent with similar plans available generally in the energy industry. Executive officers participate in the 401(k) plan on the same basis as other employees.

Supplemental Executive Retirement Plan. In addition to the 401(k) plan described above, Company officers, including all of the executive officers, and other key employees are eligible to participate in the Company's Post-2004 Supplemental Executive Retirement Plan (Post-2004 SERP). In connection with the adoption of the Post-2004 SERP, the Company suspended contributions to its previous SERP (SERP), except for guaranteed interest contributions discussed in the narrative disclosure following the Nonqualified Deferred Compensation Table. The SERP and Post-2004 SERP were implemented to allow Company officers to defer

additional pre-tax compensation for retirement without regard to the limits placed on 401(k) plans under the Internal Revenue Code. We believe that the Post-2004 SERP is an important tool for the retirement planning efforts of our officers. Moreover, after reviewing data from the benchmarking group, our Compensation Committee determined that the Post-2004 SERP is important to remain competitive in the compensation arena. Additional information regarding the operation of the SERP and Post-2004 SERP may be found in the footnotes and narrative disclosure following the Nonqualified Deferred Compensation Table.

Change of Control and Employment Agreements

Change of Control Employment Agreements. The Company has entered into Change of Control Employment Agreements with nine executive officers, including all of the named executive officers. After benchmarking studies performed by outside legal counsel at the request of the Compensation Committee in 1999, the Compensation Committee adopted a form of Change of Control Agreement. In 2005, the Compensation Committee again retained outside legal counsel to perform an update of the benchmarking study to determine whether the Change of Control Agreements remained competitive in the Company's industry. As a result of this analysis, the Compensation Committee revised the form of Change of Control Agreement to reduce the termination multiple for future agreements, as discussed in the section titled "Executive Compensation - Change of Control and Employment Agreements."

The Compensation Committee has determined that the Change of Control Agreements are a necessary component of our compensation package in order for us to provide competitive compensation arrangements, particularly because such agreements are standard in our industry. Moreover, we believe that the Change of Control Agreements help us to attract and retain our named executive officers by reducing the personal uncertainty and anxiety that arises from the possibility of a future business combination. We selected objective criteria to determine whether a change of control has occurred for purposes of the Change of Control Agreements in order to reduce the likelihood of a dispute in the event of a change of control and to help ensure that the agreements are triggered only under circumstances when a true transfer of control or ownership has occurred. While the Change of Control Agreements do not influence decisions regarding compensation elements, the Compensation Committee periodically reviews the terms of the Change of Control Agreements so that they remain generally consistent with those of the benchmarking group. Additional information regarding the Change of Control Agreements may be found in the section titled "Executive Compensation - Change of Control and Employment Agreements."

Employment Agreements. When the Company emerged from bankruptcy in 1987, it offered employment agreements to certain key officers. The only executive officers with the 1987 employment agreements are Messrs. Rock and Dudman. These agreements were entered into primarily as a retention tool but also because the Board of Directors felt that Messrs. Rock and Dudman could provide extraordinary and unique management and strategy skills to maintain and grow the Company. The Compensation Committee has reviewed these contracts and has concluded that they should remain in place but no longer offers new employment agreements to executive officers. Both agreements contain severance provisions that would entitle each individual to receive a lump sum payment in cash equal to his current annual base salary and bonus through the end of the employment period in the event that such individual were to be terminated by the Company (other than for cause, death or disability) or if for any reason his position is eliminated or otherwise becomes redundant, except in the event of a change of control as explained in the section titled "Executive Compensation - Change of Control and Employment Agreements."

Pension Plan. The Company has a defined benefit pension plan, which is currently frozen. The benefit accruals were frozen effective March 1, 1987, and the amount of the pension benefit was fixed for all eligible employees based only upon benefit accruals from September 1, 1985 to March 1, 1987. Any benefits under the pension plan are offset by benefits paid under a previous pension plan of the Company. Mr. Rock is the only named executive officer with any benefit accruals under the plan. Additional information regarding the plan may be found in the narrative discussion

following the Pension Benefits Table.

Stock Ownership Guidelines. Our Compensation Committee encourages stock ownership by executive management and periodically reviews the ownership levels and considers the appropriateness of implementing stock ownership guidelines. Our Compensation Committee has chosen not to require stock ownership guidelines for the executive management. However, as of March 15, 2008, the value of common stock owned by our CEO and

CFO are approximately 36 times and 19 times their current individual annual base salaries. This level of stock ownership evidences the alignment of the interests of our CEO and CFO with our investor's interests. Our Insider Trading Policy prohibits our executive officers from engaging in any hedging or monetization transactions involving Company securities.

COMPENSATION AND BENEFITS COMMITTEE REPORT ON EXECUTIVE COMPENSATION

The Compensation and Benefits Committee has reviewed and discussed the Compensation Discussion and Analysis with management. Based on such review and discussion, the Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this proxy statement.

G. Clyde Buck, *Chairman*
 Dod A. Fraser
 Robert Kelley

EXECUTIVE COMPENSATION

The following tables show compensation for services to the Company of the persons who during 2007 were the Principal Executive Officer, Principal Financial Officer, and the next three most highly compensated executive officers (the Named Executive Officers).

Summary Compensation Table

Name and Principal Position	Year	Salary (\$) (c)	Bonus \$(1) (d)	Stock Awards \$(2) (e)	Option Awards \$(2) (f)	Non-Equity Incentive Plan Compensation \$(3) (g)	Change in Pension Value and Nonqualified Deferred Compensation	All Other Compensation \$(4) (i)	Total \$(j)
							Earnings \$(5) (h)		
G. Clyde Buck, Chairman of the Board, President and Executive Vice President	2007	\$ 1,175,000	\$ 0	\$ 4,824,301	\$ 818,368	\$ 1,837,230	\$ (5)	\$ 590,552	\$ 9,245,052
	2006	\$ 1,100,000	\$ 0	\$ 3,065,813	\$ 1,744,770	\$ 2,200,000	\$ 1,446	\$ 580,903	\$ 8,692,892
Robert K. Dorman, Principal Financial Officer	2007	\$ 465,000	\$ 0	\$ 848,810	\$ 169,949	\$ 424,127	\$ 0	\$ 156,130	\$ 2,064,016
	2006	\$ 430,000	\$ 0	\$ 509,120	\$ 365,195	\$ 516,000	\$ 0	\$ 150,110	\$ 1,970,425
Robert A. McKenzie, Treasurer	2007	\$ 555,000	\$ 0	\$ 1,502,164	\$ 80,700	\$ 717,948	\$ 0	\$ 235,772	\$ 3,091,684
	2006	\$ 525,000	\$ 0	\$ 800,604	\$ 196,872	\$ 840,000	\$ 0	\$ 117,168	\$ 2,479,644

ent and Chief
 tive Officer,
 WACO

L. Dudman	2007	\$ 485,000	\$ 0	\$ 783,979	\$ 98,986	\$ 401,944	\$ 0	\$ 162,999	\$ 1,932
ent, Smith	2006	\$ 450,000	\$ 0	\$ 444,289	\$ 215,158	\$ 540,000	\$ 0	\$ 127,576	\$ 1,777
es									
. Kennedy	2007	\$ 400,000	\$ 0	\$ 817,336	\$ 169,949	\$ 92,300	\$ 0	\$ 108,785	\$ 1,588
ent and Chief	2006	\$ 375,000	\$ 0	\$ 509,120	\$ 365,195	\$ 396,450	\$ 0	\$ 113,960	\$ 1,759
tive Officer,									
n									

- (1) Performance-based cash bonuses paid pursuant to the AIP are included in column (g).
- (2) The amounts in column (e) and (f) reflect the dollar value recognized in the Company's financial statements for the fiscal years ended December 31, 2006 and December 31, 2007 per FAS 123R for equity awards made pursuant to the Company's Second Amended and Restated 1989 Long-Term Incentive Compensation Plan, ignoring the FAS 123R assumption for non-vested forfeitures. See note 14 to the consolidated financial statements included in the Company's Annual Report for the year ended December 31, 2007 for a complete description of the FAS 123R valuation for 2007, including forfeitures. The target, threshold and maximum value of equity awards granted during 2007 are shown below in the Grants of Plan-Based Awards Table.

- (3) The amounts in column (g) reflect the cash bonus awards paid to the named individuals in 2008 for the 2007 performance year under the AIP, which is discussed in more detail under the heading Compensation Discussion and Analysis Annual Cash Bonus.
- (4) The amounts in column (i) for 2007, which include Company contributions to the SERP and the 401(k) Plan and perquisites, are itemized below:

	SERP	401(k)	Perquisite Allowance(a)	Life Insurance Premiums
D. Rock	\$ 503,503	\$ 22,938	\$ 32,800	\$ 31,311
M. Dorman	\$ 117,986	\$ 15,063	\$ 21,700	\$ 1,381
D. McKenzie	\$ 175,283	\$ 25,281(b)	\$ 26,500	\$ 8,708
B. Dudman	\$ 114,310	\$ 18,438	\$ 27,143(c)	\$ 3,108
J. Kennedy	\$ 64,929	\$ 18,438	\$ 21,700	\$ 3,718

- (a) These amounts include a specified dollar amount for an annual physical, automobile allowance, financial planning and tax preparation, mobile phone, medical reimbursement, club memberships and legal counseling that may be used at the discretion of each individual. Perquisites are described in more detail under the heading Compensation Discussion and Analysis Perquisites.
- (b) Includes \$7,578 in profit sharing contributions from M-I SWACO.
- (c) Includes \$5,443 for spousal travel to accompany the executive on company business.
- (5) This amount reflects the change in pension value under the Smith International, Inc. Restated Pension Plan. Due to an increase in the discount rate to 6.33%, the change in pension value for the 2007 fiscal year was a negative \$752. The Restated Pension Plan is discussed in the narrative to the Pension Benefits Table below.

**GRANTS OF PLAN-BASED AWARDS
FOR FISCAL 2007**

The following table provides information regarding incentive awards made to the Named Executive Officers during the 2007 fiscal year.

Name	Grant Date	Estimated Possible Payouts Under Non-Equity Incentive Plan Awards(1)			Estimated Future Payouts Under Equity Incentive Plan Awards(2)			All Other Stock Awards(3)			Grant Date	Fair Value of Stock and Option Awards(4)
		Threshold	Target	Maximum	Threshold	Target	Maximum	Number of Shares or Units	Exercise Price (\$/Sh)	Number of Awards		
(a)	(b)	(\$)(c)	(\$)(d)	(\$)(e)	(#)(f)	(#)(g)	(#)(h)	(#)(i)	(#)(j)	(\$/Sh)(k)	(l)	(m)
Rock	12/4/2007				39,402	78,803	102,444					\$5,024,470
	N/A	\$ 282,000	\$ 1,410,000	\$ 2,820,000								N/A
Dorman	12/4/2007				16,011	32,022	41,629					\$2,041,720
	N/A	\$ 65,100	\$ 325,500	\$ 651,000								N/A
McKenzie	12/4/2007				16,011	32,022	41,629					\$2,041,720
	N/A	\$ 88,800	\$ 444,000	\$ 888,000								N/A
Dudman	12/4/2007				16,011	32,022	41,629					\$2,041,720
	N/A	\$ 63,050	\$ 315,250	\$ 630,500								N/A
Kennedy	12/4/2007				7,126	14,251	18,526					\$908,640
	N/A	\$ 52,000	\$ 260,000	\$ 520,000								N/A

- (1) Amounts represent possible payouts for the 2007 performance year under the AIP, which is discussed in more detail under the heading Compensation Discussion and Analysis Annual Cash Bonus. The actual payout amount is included in column (g) of the Summary Compensation Table.
- (2) Amounts represent performance-based restricted stock unit awards made in December 2007 for the 2008 performance year under the LTICP, which is discussed in more detail under the heading Compensation Discussion and Analysis Annual Performance-Based Restricted Stock Unit Award. If threshold levels of performance are not met, then no shares would be issued.
- (3) The grant date fair market value was determined in accordance with FAS 123R based on the closing price of the stock on the date of grant minus the present value of the dividend stream for the vesting period, assuming a 1-year, 2-year, and 3-year annual discount rate of 3.49%, 3.35%, and 3.35%, respectively.

**OUTSTANDING EQUITY AWARDS AT FISCAL YEAR END
FOR FISCAL 2007**

The following table shows the number of shares covered by exercisable and unexercisable options and unvested restricted stock units held by the Company's Named Executive Officers on December 31, 2007.

Grant Date (b)	Option Awards					Stock Awards			
	Number of Securities Underlying Unexercised Options (#) (c)	Number of Securities Underlying Unexercised Options (#) (d)	Number of Securities Underlying Unexercised Options (#) (e)	Exercise Price (\$)(f)	Option Expiration Date(1)(g)	Number of Shares or Units of Stock That Have Not Vested (#) (h)	Market Value of Shares or Units of Stock That Have Not Vested (\$)(i)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Rights That have Not Vested (#) (j)	Equity Incentive Plan Awards: Market Value of Unearned Shares, Units or Rights That have Not Vested (\$)(k)
12/4/2007								78,803	\$ 5,800,000
12/5/2006						82,506	\$ 6,093,068(2)		
12/6/2005						52,708	\$ 3,892,486(3)		
12/7/2004	64,500	21,500		\$ 28.13	12/7/2014(4)				
12/2/2003	105,000			\$ 19.41	12/2/2013(5)				
12/4/2007								32,022	\$ 2,300,000
12/5/2006						14,421	\$ 1,064,991(2)		
12/6/2005						8,280	\$ 611,478(3)		
12/7/2004	12,000	4,000		\$ 28.13	12/7/2014(4)				
12/2/2003	90,000			\$ 19.41	12/2/2013(5)				
12/3/2002	26,000			\$ 17.36	12/3/2012(6)				
12/4/2007								32,022	\$ 2,300,000
12/5/2006						32,864	\$ 2,427,006(2)		
12/6/2005						18,975	\$ 1,401,304(3)		
12/7/2004						150	\$ 10,928(7)		
12/7/2004		350		\$ 28.13	12/7/2014(4)				
12/9/2004	850	850		\$ 31.65(8)	12/9/2014				
12/3/2003	3,500			\$ 23.62(9)	12/3/2013				

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12/12/2002	2,800		\$ 22.57(10)	12/12/2012				
12/4/2007							32,022	\$ 2,3
12/5/2006					14,421	\$ 1,064,991(2)		
12/6/2005					8,280	\$ 611,478(3)		
12/7/2004	2,400	2,400	\$ 28.13	12/7/2014(4)				
12/9/2004		5,550	\$ 31.65(8)	12/9/2014				
12/4/2007							14,251	\$ 1,0
12/5/2006					14,421	\$ 1,064,991(2)		
12/6/2005					8,280	\$ 611,478(3)		
12/7/2004	4,000	4,000	\$ 28.13	12/7/2014(4)				
12/2/2003	22,500		\$ 19.41	12/2/2013(5)				

- (1) These are performance-based restricted stock units that vest at the rate of 33 1/3% a year, subject to satisfaction of performance criteria for the 2008 year, with vesting dates of 12/31/2008, 12/6/2009 and 12/6/2010.
- (2) These are performance-based restricted stock units that vest at the rate of 33 1/3% a year, based on satisfaction of performance criteria for the 2007 year, with vesting dates of 12/31/2007, 12/6/2008 and 12/6/2009.
- (3) These are performance-based restricted stock units that vest at the rate of 33 1/3% a year, based on satisfaction of performance criteria for the 2006 year, with vesting dates of 12/31/2006, 12/6/2007 and 12/6/2008.
- (4) These options vest at the rate of 25% a year on 12/7/2005, 12/7/2006, 12/7/2007 and 12/7/2008.
- (5) These options vested at the rate of 25% a year on 12/2/2004, 12/2/2005, 12/2/2006 and 12/2/2007.
- (6) These options vested at the rate of 25% a year on 12/3/2003, 12/3/2004, 12/3/2005 and 12/3/2006.
- (7) These are time-based restricted stock units that vest at the rate of 25% a year with vesting dates of 12/7/2005, 12/7/2006, 12/7/2007 and 12/7/2008.
- (8) These awards are Schlumberger Stock Appreciation Rights based on Schlumberger stock price appreciation. They were awarded as part of the compensation structure at M-I SWACO prior to the time the individuals became executive officers of the Company and vest at a rate of 25% per year, conditioned on continuous employment through the vest date, with vesting dates of 12/9/2005, 12/9/2006, 12/9/2007, and 12/9/2008. Maximum payout is limited to 125% of the initial value of the units subject to the award.

- (9) These awards are Schlumberger Stock Appreciation Rights based on Schlumberger stock price appreciation. They were awarded as part of the compensation structure at M-I SWACO prior to the time the individual became an executive officer of the Company and vested at a rate of 25% per year, conditioned on continuous employment through the vest date, with vesting dates of 12/3/2004, 12/3/2005, 12/3/2006, and 12/3/2007. Maximum payout is limited to 125% of the initial value of the units subject to the award.
- (10) These awards are Schlumberger Stock Appreciation Rights based on Schlumberger stock price appreciation. They were awarded as part of the compensation structure at M-I SWACO prior to the time the individual became an executive officer of the Company and vested at a rate of 20% per year, conditioned on continuous employment through the vest date, with vesting dates of 12/12/2003, 12/12/2004, 12/12/2005, 12/12/2006 and 12/12/2007.

OPTION EXERCISES AND STOCK VESTED FOR FISCAL 2007

The following table shows all stock options exercised and value received upon exercise, and all stock awards vested and value received upon vesting by the Named Executive Officers during the fiscal year ended December 31, 2007.

Name	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise	Value Realized on Exercise	Number of Shares Acquired on Vesting	Value Realized on Vesting
(a)	(b)	(c)	(d)	(e)
D. Rock			123,762	\$ 8,453,656
M. Dorman	140,000	\$ 5,591,794	21,015	\$ 1,433,947
D. McKenzie	53,952(1)	\$ 1,923,277	35,774	\$ 2,521,204
B. Dudman	99,252(1)	\$ 3,111,420	18,834	\$ 1,299,336
J. Kennedy	136,000	\$ 6,907,809	21,015	\$ 1,433,947

- (1) This amount includes the exercise of Schlumberger Stock Appreciation Rights described in more detail in the footnotes to the Outstanding Equity Awards at Fiscal Year End Table above.

PENSION BENEFITS FOR FISCAL 2007

The following table shows the number of years of credited service of and present value of accumulated benefits payable to each of the named Executive Officers under the Company's Restated Pension Plan.

Number of Years Credited Service	Present Value of Accumulated Benefit	Payments During Last Fiscal Year
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Name (a)	Plan Name (b)	(#) (c)	(\$) (d)	(\$) (e)
D. Rock	Smith International, Inc. Restated Pension Plan	1.5	\$66,551	\$0
M. Dorman	N/A	N/A	N/A	N/A
D. McKenzie	N/A	N/A	N/A	N/A
B. Dudman	N/A	N/A	N/A	N/A
J. Kennedy	N/A	N/A	N/A	N/A

The Company has a defined benefit pension plan (the Restated Pension Plan), which is currently frozen. The benefit accruals were frozen effective March 1, 1987, and the amount of the pension benefit was fixed for all eligible employees based only upon benefit accruals from September 1, 1985 to March 1, 1987. Since benefit accruals under the Restated Pension Plan have been frozen since March 1, 1987, the years of service for the Named Executive Officers include only the period from September 1, 1985 to March 1, 1987. The accumulated benefit presented above assumes a retirement age of 65, no pre-retirement decrements, a post-retirement mortality assumption based

on the RP2000 Combined Healthy Mortality Table Projected by Scale AA to 2015, and payment in the form of a single life annuity.

**NONQUALIFIED DEFERRED COMPENSATION
FOR FISCAL 2007**

The following table and narrative disclosure provides information regarding nonqualified deferred compensation with respect to each Named Executive Officer.

Name	Executive Contributions in Last FY	Registrant Contributions in Last FY	Aggregate Earnings in Last FY	Aggregate Withdrawals/ Distributions	Aggregate Balance at Last FYE
(a)	(\$) (b)	(\$)(1) (c)	(\$) (d)	(\$) (e)	(\$) (f)
D. Rock	\$ 650,000	\$ 503,503	\$ 692,564	\$ 0	\$ 15,206,555
M. Dorman	\$ 82,950	\$ 117,986	\$ 69,460	\$ 0	\$ 1,608,955
D. McKenzie	\$ 111,000	\$ 175,283	\$ 161,957	\$ 0	\$ 3,558,539
B. Dudman	\$ 219,000	\$ 114,310	\$ 234,124	\$ 0	\$ 3,042,756
J. Kennedy	\$ 0	\$ 64,929	\$ 129,883	\$ 0	\$ 2,709,168

- (1) Includes age-weighted and matching contributions made by the Company and additional Company contributions, if any, as explained below. These amounts are reported as All Other Compensation for each named executive officer in the Summary Compensation Table.

Smith International, Inc. Post-2004 Supplemental Executive Retirement Plan. The Smith International, Inc. Post-2004 Supplemental Executive Retirement Plan (the "Post-2004 SERP") is a non-qualified, deferred compensation plan, for the benefit of officers and certain other eligible employees of the Company as selected by the Compensation Committee. Participants may contribute, on a pre-tax basis, up to 100% of their cash compensation, as defined in the Post-2004 SERP. Distributions may generally be made either as a lump sum or installment payments following the participant's termination of employment due to death, disability, retirement or other separation from service. Distributions may also be made on a limited basis and to the extent necessary as a lump sum upon the occurrence of the participant's unforeseeable financial emergency as approved by the Compensation Committee. The Post-2004 SERP also provides for Company contributions, as follows:

Age-Weighted Contributions. The Company provides an age-weighted contribution percentage ("AWCP") ranging from 2% to 6% of qualified compensation, less any age-weighted contributions made to the participant's 401(k) account. The Post-2004 SERP provides that the AWCP for executive officers is 6% of qualified compensation regardless of age. The difference between a participant's (i) Total 401(k) Compensation and (ii) Net 401(k) Compensation is multiplied by the AWCP to compute the age-weighted contribution. Total 401(k) Compensation generally means the total of all cash amounts paid by the Company to a participant, including deferred amounts. Net 401(k) Compensation generally means Total 401(k) Compensation less participant contributions to the Post-2004 SERP, but not to exceed the limit set under the Internal Revenue Code.

Matching Contributions. The Company provides a performance-based matching contribution ranging from zero to 100% of salary deferrals that mirrors the matching formulas in effect for the Company's 401(k) Plan, but without

regard to certain Code limits applicable to the 401(k) Plan. Matching contributions for all plan participants are limited to 6% of Total 401(k) Compensation, less any performance-based matching contributions made in their individual 401(k) account. Executive officers receive 100% matching contributions subject to the same limitation.

Additional Company Contributions. Deferred funds are placed with the fund trustee and invested at the discretion of the participant in a variety of funds, including a money market fund. The Company guarantees that the deferrals invested in the money market fund will yield interest at 120% of the long-term applicable federal rate (AFR). Therefore, in addition to the contributions described above, for the portion of each participant s account invested in the money market fund that is earning less than 120% of AFR, the Company makes a contribution equal to the difference in interest between the money market fund rate actually earned by the money market fund and 120% of the AFR, which contribution is credited to the participant s account.

Discretionary Profit Sharing Contributions. The Compensation and Benefits Committee may, in its discretion, determine the amount of any profit sharing contribution for a plan year and how that amount is to be allocated among the accounts of the Post-2004 SERP participants.

In the event of insolvency or bankruptcy, all assets allocable to the Post-2004 SERP are available to satisfy the claims of all general unsecured creditors of the Company. The Company established a grantor trust to serve as a source of funds from which it can satisfy its obligations under the Post-2004 SERP. Participants in the Post-2004 SERP will have no rights to any assets held in the trust, except as general creditors of the Company. A participant's rights to any amounts credited to an account under the Post-2004 SERP cannot be anticipated, alienated, sold, assigned, pledged, encumbered or charged by the participant and may only pass upon the participant's death pursuant to a beneficiary designation made by the participant under the Post-2004 SERP. The Company may, by action of the Compensation and Benefits Committee, terminate the Post-2004 SERP with respect to future contributions; provided, however, such termination shall not affect any participant's right to receive any distribution due under the Post-2004 SERP.

The Post-2004 SERP will be interpreted by the Compensation and Benefits Committee in such manner as necessary to comply with the requirements of Code Section 409A and the authority issued thereunder.

Smith International, Inc. Supplemental Executive Retirement Plan. In connection with the adoption of the Post-2004 SERP and Code Section 409A, the Company suspended contributions to the SERP effective December 31, 2004, other than such contributions that were earned and vested as of December 31, 2004. However, the Company may be required to make contributions to participants' accounts to guarantee an investment return equal to 120% of the AFR on deferrals invested in the money market fund, in the same manner as explained above.

With respect to Company insolvency or bankruptcy, participant's rights, beneficiary designations and plan termination, the SERP is in all material respects the same as the Post-2004 SERP.

Change of Control and Employment Agreements

Employment Agreements. As discussed in Compensation Discussion and Analysis above, the Company has employment agreements from 1987 with Messrs. Rock and Dudman. These agreements have an initial term of three years and are automatically extended for an additional year at each anniversary date. Automatic renewals may not be suspended by the Company without triggering severance. The agreements automatically terminate when the respective executive reaches age 65. Each employment agreement contains salary and other conditions of employment and entitles the employee to participate in the Company's bonus program and other benefit programs. If the employment of Mr. Rock or Mr. Dudman is terminated by the Company (other than for cause, death or disability) or if for any reason his position is eliminated or otherwise becomes redundant, Mr. Rock or Mr. Dudman, as applicable, would be entitled to receive a lump sum payment in cash equal to his current annual base salary and bonus through the end of the employment period; provided, however, that in the event of a change of control, the Change of Control Agreements discussed elsewhere in this proxy statement would control, except with respect to any accrued obligations under the employment agreements that were not fully accrued under the applicable Change of Control Agreement.

Change of Control Employment Agreements. The Company has entered into Change of Control Employment Agreements (Change of Control Agreements) with nine executive officers, including all of the Named Executive Officers. In the event of a change of control of the Company (as defined in the Change of Control Agreements), the Change of Control Agreements provide for the continued employment of the executive officers for a period of three years and provide for the continuation of salary and benefits.

If, after a change of control event, the executive is terminated by the Company (other than for cause, death or disability), or if the executive elects to terminate his or her employment for Good Reason (as defined in the Change of Control Agreements), the executive is entitled to receive the following:

A lump sum cash payment equal to:

The current annual base salary through the date of termination to the extent not paid and highest annual bonus (as explained below) prorated for the number of days worked in the year (referred to as Accrued Obligations).

Any compensation previously deferred by the executive and any accrued vacation pay to the extent not paid.

The sum of the executive's annual base salary and highest annual bonus (as explained below) multiplied by the termination multiple applicable to the executive (as explained below), with annual base salary to be calculated as 12 times the highest monthly base salary paid or payable to the executive during the preceding 12 months.

Any actuarial difference in the SERP benefit the executive would have received had the executive's employment continued for the number of years after the date of the executive's termination multiplied by the termination multiples applicable to the executive.

For these calculations, the annual bonus is calculated as the highest annual bonus paid or payable to the executive for the last three full fiscal years prior to the effective date of the change of control event.

Continued coverage under applicable welfare and benefit plans for a number of years equal to the termination multiple applicable to the executive.

Outplacement services for the executive.

Any other amounts or benefits required to be paid or provided under any other Company plan (referred to as Other Benefits).

A tax gross-up of any excise tax due under the Internal Revenue Code.

If the executive's employment is terminated by reason of the executive's death or disability, the executive or the estate of the executive shall be entitled to payment of Accrued Obligations and Other Benefits as explained above.

Termination Multiple. The Change of Control Agreements for Messrs. Rock and Kennedy and Ms. Dorman include a termination multiple of three times for termination at any time within three years after the change of control event occurs. The Change of Control Agreements for Messrs. McKenzie and Dudman include a termination multiple of three times for termination of employment in year one after the change of control event; two times in year two; and one time in year three.

Stock Incentive Plan. The Company's Second Amended and Restated 1989 Long-Term Incentive Compensation Plan provides for the vesting of all outstanding stock options and the satisfaction of all restrictions and conditions on restricted stock and other stock-based awards and the full vesting at 100% target levels of all performance-based awards, as of the day immediately preceding the change of control date.

Potential Payments upon a Change of Control. The table below shows potential payments if an executive is terminated other than for cause or voluntary termination after a change of control event. The amounts assume that the

change of control event and termination of employment were both effective on December 31, 2007, and are estimates that reflect the amounts that would be paid and the incremental value of benefits that would be enhanced through accelerated vesting of options and stock awards. The value of equity awards is based on Smith's closing market price of \$73.85 on December 31, 2007, the last trading day before year end. As discussed above, the accelerated vesting of outstanding equity awards occurs on the day immediately preceding the change of control date, regardless of whether the executive is terminated or terminates his or her employment following the change of control event. The table also assumes that the executive has been paid in full for salary due for the fiscal year and has no deferred compensation, pro-rated perquisites payments or accrued vacation due for the year. Because the termination is assumed to be on the same day as the change of control, amounts shown in this column use a 3x

termination multiple for all executives. For Messrs. McKenzie and Dudman, if the termination of employment occurred in year two after the change of control event, the termination multiple would be 2x and if the termination of employment occurred in year three after the change of control event, the termination multiple would be 1x.

Name (a)	Pro Rata					Welfare and Benefit Plan Coverage and Outplacement		Tax (h)	Total (i)
	Bonus for Current Fiscal Year(1) (b)	Salary and Bonus Severance(2) (c)	Option Awards(3) (d)	Stock Awards(4) (e)	SERP Benefits(5) (f)	Services(6) (g)			
J. Rock	\$ 1,837,230	\$ 11,985,000	\$ 982,980	\$ 15,805,155	\$ 977,094	\$ 92,745	\$ 0	\$ 31,680,204	
L. Dorman	\$ 424,127	\$ 3,348,000	\$ 182,880	\$ 4,041,294	\$ 224,584	\$ 92,745	\$ 2,048,048	\$ 10,361,678	
J. McKenzie	\$ 717,948	\$ 4,329,000	\$ 16,002	\$ 6,204,062	\$ 329,964	\$ 92,745	\$ 2,810,211	\$ 14,499,932	
J. Dudman	\$ 401,944	\$ 3,346,500	\$ 109,728	\$ 4,041,294	\$ 294,925	\$ 92,745	\$ 1,863,654	\$ 10,150,790	
J. Kennedy	\$ 92,300	\$ 2,760,000	\$ 182,880	\$ 2,728,905	\$ 234,021	\$ 92,745	\$ 0	\$ 6,090,851	

- (1) Because the termination is assumed to be effective on December 31, 2007, the amount shown represents bonus for the full year.
- (2) Amounts shown in column (c) assume a 3x termination multiple for all executives.
- (3) Amounts shown in column (d) represent the value of unvested options that would accelerate upon a change of control based on the difference between the closing price of Smith's common stock at the end of fiscal 2007 and the exercise price of the respective options. The number of vested and exercisable options outstanding for each individual on December 31, 2007 is included in the Outstanding Equity Awards at Fiscal Year End table.
- (4) Amounts shown in column (e) represent the value of unvested performance-based restricted stock units at the target performance level and unvested restricted stock units, the vesting of which would accelerate upon a change of control based on the closing price of Smith's common stock at the end of fiscal 2007.
- (5) Amounts shown in column (f) represent the excess of (i) the actuarial equivalent of the benefit under the Company's current SERP and previous SERP and (ii) the actuarial equivalent of the executive's actual benefit, if any, as of the date of termination, assuming that the executive's base salary and contribution amounts remain at the same level as the highest monthly salary paid during fiscal year 2007. Amounts assume a 3x termination multiple for all executives.
- (6) Amounts shown in column (g) represent the continuation of benefits to the executive and the executive's family equal to those that would have been provided to them in accordance with the plans if (i) the executive's employment had not terminated and (ii) the executive had remained employed and retired on the last day of such period, assuming full family coverage at the lowest deductible amounts under all benefit plans for each individual. Amounts assume benefits for three years for all executives. This amount also includes \$50,000 in outplacement services for each executive.

In the event of the executive's termination of employment due to death or disability on December 31, 2007, payments would include the amounts indicated in column (b), (d) and (e) above.

**DIRECTOR COMPENSATION
FOR FISCAL 2007**

Set forth below is a summary of the dollar values of the total annual compensation attributable to each non-employee director's service to Smith during 2007.

Name (a)	Fees Earned or Paid in Cash (\$) (b)	Stock Awards (\$) (c)	Option Award Compensation (\$) (d)	Non-Equity Incentive Plan Compensation (\$) (e)	Change in Pension Value and Nonqualified Deferred Compensation Earnings (\$) (f)	All Other Compensation (\$) (g)	Total (\$) (h)
G. Clyde Buck	\$ 107,750	\$ 152,610	\$ 0	\$ 0	\$ 0	\$ 0	\$ 260,360
Dod A. Fraser	\$ 117,750	\$ 152,610	\$ 0	\$ 0	\$ 0	\$ 0	\$ 270,360
James R. Gibbs	\$ 121,000	\$ 152,610	\$ 0	\$ 0	\$ 0	\$ 0	\$ 273,610
Robert Kelley	\$ 100,750	\$ 152,610	\$ 0	\$ 0	\$ 0	\$ 1,000(1)	\$ 254,360
Jerry W. Neely(2)	\$ 37,750	\$ 298,290(3)	\$ 0	\$ 0	\$ 0	\$ 0	\$ 336,040
John Yearwood	\$ 90,679	\$ 152,610	\$ 0	\$ 0	\$ 0	\$ 0	\$ 243,289

(1) This amount represents a matching educational gift made on behalf of Mr. Kelley.

(2) Mr. Neely served as a director until April 25, 2007.

(3) This amount includes the FAS 123R value of Common Stock, as of April 25, 2007, issued to Mr. Neely as a result of 24,000 restricted stock units vesting upon his retirement as a director.

As an employee of the Company, Mr. Carroll receives no separate fees for his service as a director. His total compensation for services rendered to the Company during 2007 was \$1,903,841, which includes base salary of \$200,004, the FAS 123R value of option awards made pursuant to the LTICP of \$1,102,066, the FAS 123R value of restricted stock unit awards made pursuant to the LTICP of \$378,655, contributions to the SERP of \$121,638, contributions to the 401(k) of \$22,938, life insurance premiums of \$5,040 and a lump sum in the amount of \$73,500 for perquisites pursuant to Mr. Carroll's employment agreement.

Mr. Neely has served as an Advisory Director at the request of the Board since his retirement as a director. In 2007, as compensation for his services as Advisory Director, Mr. Neely was paid an annual cash retainer of \$25,000 and \$38,000 for Board and committee meetings attended in person or telephonically.

Directors Compensation

Employee directors receive no additional compensation other than their normal salary for serving on the Board. Non-employee directors receive \$50,000 annually and \$2,000 for each Board meeting attended. In addition, they are paid \$10,000 per year for chairing a committee (other than the chairman of the Audit Committee who is paid \$15,000 per year) and \$2,000 for each committee meeting attended even if they are not members of such committee. The lead director is paid \$15,000 per year. Expenses for Company related business travel are either paid or reimbursed by the Company. During 2007, non-employee directors also received an initial grant of shares, upon first election or appointment, along with an annual grant of shares of Common Stock, each with a value of approximately \$150,000. Effective January 2008, the value of the initial and annual grants is approximately \$200,000.

Non-Employee Director Programs

The Company terminated its Directors Retirement Plan in 1998. The Company issued restricted stock unit grants to each of the non-employee directors in 1999 to fund the actuarial value of their accrued benefits under the retirement plan. These grants of 24,000 shares (adjusted for the two-for-one stock splits on June 20, 2002 and August 24, 2005) will vest upon retirement after ten years of service as a director. Cash dividends are not paid and do not accrue on the unvested units. The two directors with outstanding restricted stock units are Messrs. Buck and Gibbs.

Director Stock Ownership Guidelines

The Board has established non-employee director stock ownership guidelines to align the interests of the directors with those of our stockholders and further promote Smith's commitment to sound corporate governance. The guidelines are premised upon every non-employee director holding a number of shares of common stock equaling five times the director's annual cash retainer, within three years of the date the guidelines become effective with respect to said individual.

ADDITIONAL INFORMATION ABOUT OUR DIRECTORS AND EXECUTIVE OFFICERS

Certain Relationships and Related Transactions

The Audit Committee has adopted a written policy which provides guidelines for monitoring and approving transactions with related parties. Pursuant to the policy, related parties include all executive and operating officers, members of the Board of Directors and stockholders who own more than 5% of our common stock. Transactions with related parties that are entered into at prevailing prices and which comply with standard terms and conditions require no prior approval, except that all transactions with the Chief Executive Officer or Chief Financial Officer require pre-approval from the Nominating and Corporate Governance Committee. Transactions with related parties that do not reflect prevailing prices and do not comply with standard terms and conditions require pre-approval from the Chief Executive Officer or Chief Financial Officer and the Nominating and Corporate Governance Committee.

We have not engaged in any transaction, or series of similar transactions, since the beginning of 2007, nor is there any currently proposed transaction, or series of similar transactions, to which Smith or any of its subsidiaries was or is to be a participant, in which the amount involved exceeds \$120,000 and in which any of Smith's directors or executive officers, members of their immediate family or any stockholder who owns more than 5% of our common stock had, or will have, a direct or indirect material interest.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Exchange Act requires the Company's officers and directors, and persons who own more than 10% of the Company's outstanding shares of Common Stock (collectively, Section 16 Persons), to file with the SEC initial reports of ownership and reports of changes in ownership of Common Stock and other equity securities. Section 16 Persons are required by Commission regulations to furnish the Company with copies of all Section 16(a) reports they file.

Based solely on its review of the copies of such reports received by it, or written representations from certain Section 16 Persons that all Section 16(a) reports required to be filed for such persons had been filed, the Company believes that during 2007 the Section 16 Persons complied with all Section 16(a) filing requirements applicable to them, except that Mr. Anderson filed one late report disclosing shares purchased pursuant to a dividend reinvestment program that had been inadvertently omitted; Mr. Gibbs filed one late report disclosing the continuation of a gift to his daughter that had been inadvertently omitted and Mr. Neely filed one late report disclosing a gift of shares via inheritance to his wife that had been inadvertently omitted.

PROPOSAL 2: APPROVAL OF THE SMITH INTERNATIONAL, INC. THIRD AMENDED AND RESTATED 1989 LONG-TERM INCENTIVE COMPENSATION PLAN

At the meeting, you will be asked to approve an amendment and restatement to the Smith International, Inc. Second Amended and Restated 1989 Long-Term Incentive Compensation Plan (the Plan), which incorporates previous

amendments and increases by 4,000,000 the number of shares of Common Stock reserved for the Plan. On March 14, 2008, the last reported closing price of our Common Stock on the New York Stock Exchange Composite Tape was \$63.10.

The Plan was originally approved by the stockholders at the May 9, 1989 Annual Meeting. Since 1989, as adjusted to reflect stock splits, a total of 29,040,000 shares of Common Stock have been reserved for issuance under the Plan. On February 6, 2008, the Board of Directors approved an amendment to the Plan to reserve an additional 4,000,000 shares of Common Stock reserved for issuance under the Plan. At the Annual Meeting, you will be asked to approve the proposed amendment to the Plan described above.

Of the total shares authorized for issuance under the Plan, at December 31, 2007, all but 1,074,185 shares have been awarded in the form of stock options or restricted stock. Should the stockholders approve the proposed amendment to the Plan, a total of approximately 5,074,185 shares, or approximately 2.5% of the Company's outstanding Common Stock, would be reserved for issuance under the Plan. In addition, of the shares that have already been awarded under the Plan, 3,673,209 shares remained to be issued upon exercise of outstanding stock options or vesting of previously granted restricted stock unit awards.

The Board of Directors has found that restricted stock unit awards granted to employees have been highly effective in recruiting and retaining competent personnel. The Board of Directors believes that the growth of the Company is dependent upon its ability to attract, employ and retain executives and employees of outstanding ability who will dedicate their maximum productive efforts toward the advancement of the Company. The growing competition among companies for capable managers makes it necessary for the Company to maintain a strong and competitive incentive program. The additional 4,000,000 shares will allow the Company to continue its long-term incentive program and to recognize the increased pool of employees eligible to participate. The Company intends to continue to make awards at similar levels and on the same criteria as it has done under the Plan.

Description of the Plan

The following summary describes briefly the principal features of the Plan, and is qualified in its entirety by reference to the full text of the Plan, which is provided as Appendix A to this Proxy Statement.

Purpose. The purpose of the Plan is to foster and promote the long-term financial success of the Company and to increase stockholder value by: (a) encouraging the commitment of selected key Employees (as defined in the Plan), (b) motivating superior performance of key Employees by means of long-term performance related incentives, (c) encouraging and providing key Employees with a program for obtaining ownership interests in the Company which link and align their personal interests to those of the Company's stockholders, (d) attracting and retaining key Employees by providing competitive compensation opportunities, (e) enabling key Employees to share in the long-term growth and success of the Company, (f) providing additional incentives for securing and retaining qualified individuals who are not employees of the Company to serve on the Board of Directors of the Company (Outside Directors), and (g) to enhance the future growth of the Company by furthering Outside Directors' alignment with the interests of the Company and its stockholders.

Awards Under the Plan. The Plan provides for the following types of awards: (a) nonqualified stock option; (b) stock appreciation right; (c) common stock to Outside Directors; (d) restricted stock (including performance-based); (e) restricted stock unit (including performance-based) (f) stock-based award; and (g) any combination of the foregoing. The Plan permits the grant of awards subject to performance objectives in order to qualify for the performance-based exception within Section 162(m) of the Internal Revenue Code. As of March 15, 2008, nonqualified stock options, common stock and restricted stock units (including performance-based) have been awarded under the Plan.

Plan Administration. The Plan is administered by the Compensation and Benefits Committee. However, the Independent Directors of the Board constitutes the Committee under the Plan with respect to awards to Outside Directors. Future awards are based on future performance or future stock price and, therefore, are not currently determinable. Please see the section entitled "Compensation Discussion and Analysis" for more information regarding future grants to the named executive officers; the Outstanding Equity Awards at Fiscal Year End Table for more information regarding past grants to the named executive officers; and the Director Compensation Table and related narrative discussion for more information regarding grants to outside directors.

Participation and Eligibility. All full-time salaried employees of the Company whom the Compensation and Benefits Committee determines are in a position to contribute to the growth, development or financial success of the Company and Outside Directors are eligible to receive awards under the Plan. Common stock awards are only available to Outside Directors.

Shares Subject to Awards Under the Plan. Since 1989, as adjusted to reflect stock splits, a total of 29,040,000 shares of Common Stock have been reserved for issuance under the Plan. Upon expiration, cancellation or termination of unexercised awards granted under the Plan or forfeiture of shares of restricted stock, the shares of Common Stock subject to such awards will again be available for the grant of awards under the Plan. If any change

occurs in the capitalization of the Company, such as a stock dividend or stock split, or if a merger takes place in which the Company is the surviving corporation, the Board or the Compensation Committee may take such action as it deems appropriate so that the value of each outstanding award shall not be adversely affected by such corporate event.

General Terms of the Awards. The specific terms and conditions of each award, including the vesting and termination of such awards, shall be fixed by the Compensation and Benefits Committee pursuant to the Plan at the time the award is granted. Subject to exceptions, determined by the Compensation and Benefits Committee pursuant to the Plan, the maximum stock based award that may be granted to a Plan participant in a given year is 1,000,000 shares. The grant price of an option or stock appreciation right (SAR) may not be less than 100% of the fair market value of our Common Stock on the date of grant of the option. Pursuant to the provisions of the Plan and New York Stock Exchange rules, awards under the Plan may not be re-priced without stockholder approval.

Federal Income Tax Consequences Associated with Awards Granted Under the Plan. The following is a general summary as of the date of this Proxy Statement of the United States federal income tax consequences associated with the grant of awards under the Plan. The federal tax laws may change and the federal, state and local tax consequences for any participant will depend upon his or her individual circumstances, thus the tax consequences for any particular individual may be different. Also, this information may not be applicable to any employees of foreign subsidiaries or to participants who are not residents of the United States.

As discussed above, several different types of incentive awards may be issued under the Plan. The tax consequences related to the issuance of each type of award is discussed separately below.

Nonqualified Stock Options and Stock Appreciation Rights (SARs). Nonqualified stock options granted under the Plan are not intended to qualify as incentive stock options and will not qualify for any special tax benefits to the optionee. A participant receiving a nonqualified stock option or SAR that has been issued with an exercise price not less than the fair market value of the Company's common stock on the grant date will not recognize income and the Company will not be allowed a deduction at the time such an option is granted. When a participant exercises a nonqualified stock option or SAR, the difference between the exercise price and any higher market value of the stock on the date of exercise will be ordinary income to the participant. When a participant disposes of shares acquired by the exercise of the option or SAR, any additional gain or loss will be a capital gain or loss.

In general, there will be no federal income tax deduction allowed to the Company upon the grant or termination of a nonqualified stock option or SAR or a sale or disposition of the shares acquired upon exercise of the stock option or SAR. However, upon the exercise of a nonqualified stock option or SAR, the Company will be entitled to a deduction for federal income tax purposes equal to the amount of ordinary income that the participant is required to recognize as a result of the exercise, provided that the deduction is not otherwise disallowed under the Internal Revenue Code.

Restricted Stock Awards, Restricted Stock Unit Awards and Stock-Based Awards. Generally, the recipient of a restricted stock award or restricted stock unit award has no federal income tax consequences at the time of grant. Rather, at the time the shares are vested and no longer subject to a substantial risk of forfeiture, the participant will recognize ordinary income to the extent of the excess of the fair market value of the stock on the date the risk of forfeiture ceases over the amount paid, if any, by the participant for such stock. For a restricted stock award only, the participant may instead elect to be taxed at the time of grant by making an election under Section 83(b) of the Internal Revenue Code.

In the year that the recipient of a restricted stock award, restricted stock unit award or stock-based award recognizes ordinary taxable income in respect of such award, the Company will be entitled to a deduction for federal income tax purposes equal to the amount of ordinary income that the participant is required to recognize, provided that the deduction is not otherwise disallowed under the Internal Revenue Code. Upon disposition of the shares received, the

gain or loss recognized by the participant will be treated as capital gain or loss.

Performance-Based Awards. With certain exceptions, Section 162(m) of the Internal Revenue Code denies a deduction to the Company for compensation paid to certain executive officers in excess of \$1 million per executive per taxable year. One such exception applies to certain performance-based compensation as described in Section 162(m), and certain awards granted under the Plan will be intended to qualify as performance-based compensation. The Plan contains provisions consistent with the requirements for performance-based compensation under Section 162(m). However, the Compensation and Benefits Committee may award non-deductible compensation when such grants are in the best interest of the Company, balancing tax efficiency with long-term strategic objectives.

Section 409A. Section 409A of the Internal Revenue Code provides certain new requirements for non-qualified deferred compensation arrangements. These include requirements with respect to an individual's election to defer compensation and the individual's selection of the timing and form of distribution of deferred compensation. Section 409A also generally provides that distributions must be made on or after the occurrence of certain events (e.g., the individual's separation from service, a predetermined date, or the individual's death). Section 409A imposes restrictions on an individual's ability to change his or her distribution timing or form of distribution, after the compensation has been deferred.

Awards granted under the Plan with a deferral feature will be subject to the requirements of Section 409A. If an award is subject to and fails to satisfy the requirements of Section 409A, the recipient of that award may recognize ordinary income on the amounts deferred under the award, to the extent vested, which may be prior to when the compensation is actually or constructively received. Also, if an award that is subject to Section 409A fails to comply with Section 409A, an additional 20% federal income tax is imposed on compensation recognized as ordinary income, as well as interest on such deferred compensation.

ERISA. The Company believes that the Plan is not subject to any provisions of the Employee Retirement Income Security Act of 1974 (ERISA). The Plan is not a qualified plan under Section 401(a) of the Internal Revenue Code.

Amendment of the Plan. The Board of Directors may terminate, modify or amend the Plan at any time without stockholder approval, except for amendments that (a) change the class of persons eligible to receive awards; (b) extend the term of the Plan; (c) decrease the authority granted to the Committee under the Plan; (d) increase the number of shares subject to the Plan or (e) require stockholder approval under New York Stock Exchange listing standards or the Internal Revenue Code in order to maintain listing requirements or favorable tax advantages or qualifications.

Required Approval. The affirmative vote of a majority of the shares represented at the Annual Meeting and entitled to vote will be sufficient to approve the Plan.

WE RECOMMEND THAT YOU VOTE FOR APPROVAL OF THE THIRD AMENDED AND RESTATED 1989 LONG-TERM INCENTIVE COMPENSATION PLAN.

EQUITY COMPENSATION PLAN INFORMATION

The following table shows information as of December 31, 2007, with respect to the Smith International, Inc. Second Amended and Restated 1989 Long-Term Incentive Compensation Plan:

Plan Category	(a) Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants and Rights	(b) Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	(c) Number of Securities Remaining Available for Future issuance under Equity Compensation Plans (Excluding Securities Reflected in Column(a))

Equity compensation plans approved by security holders	3,673,209(1)	\$20.04(2)	1,074,185(3)
Equity compensation plans not approved by security holders	Not applicable	Not applicable	Not applicable
Total	3,673,209(1)	\$20.04(2)	1,074,185(3)

(1) Includes an aggregate of 2,077,538 restricted stock units and performance-based restricted stock units awarded to employees; 1,547,671 non-qualified stock options awarded to employees; and 48,000 restricted stock units to be awarded to directors upon their retirement from the board.

(2) Weighted average exercise price of outstanding options; excludes restricted stock units and performance-based restricted stock units.

**PROPOSAL 3: APPROVAL OF AN AMENDMENT TO THE RESTATED
CERTIFICATE OF INCORPORATION TO INCREASE THE NUMBER
OF AUTHORIZED SHARES OF COMMON STOCK**

At the Annual Meeting, you will be asked to approve an amendment to the Restated Certificate of Incorporation of the Company to increase the number of shares of Common Stock that the Company has authority to issue from 250,000,000 to 500,000,000. The number of shares of preferred stock authorized would not be changed by this amendment, nor would the par value of either the Common Stock or the preferred stock be affected in any way.

As of March 15, 2008, 217,855,448 shares of Common Stock were issued (including 17,038,887 shares held as treasury stock) and an aggregate of 4,478,162 shares were reserved for issuance under the Company's Second Amended and Restated 1989 Long-Term Incentive Compensation Plan (the Plan). As of March 15, 2008, 27,666,390 shares were unreserved. If the stockholders approve Proposal 2, then 8,478,162 shares will be reserved for issuance under the Plan and 23,666,390 shares will be unreserved. If the proposed amendment to the restated certificate of incorporation is approved, an aggregate of 273,666,390 shares of Common Stock will be available for issuance. The Company does not have any current plans, agreements or understandings to issue stock that would involve any of the shares of Common Stock resulting from the increase in the number of authorized shares.

On February 6, 2008, the Board of Directors of the Company adopted a resolution approving the amendment to increase the number of authorized shares of Common Stock, subject to stockholder approval. The Board of Directors of the Company believes that it is desirable to have the additional authorized shares of Common Stock available for possible future stock dividends or splits, financing and acquisition transactions, employee benefit plans and other general corporate purposes. Having additional authorized shares of Common Stock available for issuance in the future will give the Company greater flexibility and may allow these shares to be issued without the expense and delay of a special meeting of the stockholders. All authorized but unissued shares of Common Stock, including the additional shares of Common Stock authorized by the proposed amendment, will be available for issuance without further authorization of the stockholders, unless stockholder action is required by applicable law or the rules of a stock exchange on which the Common Stock is listed.

Issuing additional shares of Common Stock or rights to acquire additional shares of Common Stock could have the effect of diluting the stock ownership, earnings per share and voting power of existing stockholders, except in pro rata distributions such as stock dividends and stock splits. The proposed amendment also may have the effect of discouraging attempts to take over control of the Company, as additional shares of Common Stock could be issued to dilute the stock ownership and voting power of, or increase the cost to, a party seeking to obtain control of us. The proposed amendment is not being proposed in response to any known effort or threat to acquire control of the Company and is not part of a plan by management to adopt a series of amendments to the Restated Certificate of Incorporation and Bylaws having an anti-takeover effect.

The affirmative vote of a majority of the outstanding shares of Common Stock is required to approve the proposed increase in the authorized number of shares of Common Stock. Accordingly, abstentions and broker non-votes applicable to shares present at the Annual Meeting will have the same effect as votes cast against approval of the proposed amendment. If the proposed amendment is approved, the first sentence of Article FOURTH of the Company's Restated Certificate of Incorporation will read as follows:

FOURTH: The total number of shares of stock that the Corporation shall have authority to issue is 505,000,000, consisting of 500,000,000 shares of Common Stock, par value \$1.00 per share (the Common Stock), and 5,000,000 shares of Preferred Stock, par value \$1.00 per share (the Preferred Stock).

**WE RECOMMEND THAT YOU VOTE FOR APPROVAL OF
THE AMENDMENT TO THE RESTATED CERTIFICATE OF INCORPORATION TO
INCREASE THE NUMBER OF AUTHORIZED SHARES OF COMMON STOCK.**

**PROPOSAL 4: RATIFICATION OF DELOITTE & TOUCHE LLP
AS INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Audit Committee has selected Deloitte & Touche LLP as its independent registered public accounting firm to audit the books and records of the Company for its fiscal year ending December 31, 2008. The services of Deloitte & Touche LLP will include the audit of the effectiveness of internal controls over financial reporting. The Company has been advised by Deloitte & Touche LLP that the firm has no relationship with the Company or its subsidiaries other than that arising from the firm's engagement as independent registered public accountants and, in limited circumstances, tax advisors. Deloitte & Touche LLP has audited the Company's financial statements since April 15, 2002.

Deloitte & Touche LLP has offices in or convenient to most of the locations in the world where the Company and its subsidiaries operate. Representatives of Deloitte & Touche LLP are not expected to be present at the Annual Meeting, will not have the opportunity to make a statement and will not be available to respond to questions.

Fees Paid to Deloitte & Touche LLP

During fiscal years 2007 and 2006, the Company incurred the following fees for services performed by Deloitte & Touche LLP:

	2007	2006
Audit Fees	\$ 4,976,000	\$ 4,890,000
Audit-Related Fees	348,000	104,000
Tax Fees	0	35,000
All Other Fees	0	0
Total	\$ 5,324,000	\$ 5,029,000

Audit Fees. This category includes the audit of Smith's annual financial statements and internal control over financial reporting as required by Section 404 of the Sarbanes-Oxley Act, audits of statutory accounts in certain non-U.S. jurisdictions, review of financial statements included in Smith's quarterly reports on Form 10-Q and services that are normally provided by the independent registered public accountants in connection with statutory and regulatory filings or engagements for those fiscal years. This category also includes the audit of the combined financial statements of M-I SWACO, the Company's majority-owned joint venture.

Audit-Related Fees. This category consists of assurance and related services by Deloitte & Touche LLP that are reasonably related to the performance of the audit or review of Smith's financial statements and are not reported above under Audit Fees. The services for the fees disclosed under this category primarily relate to the audit of various U.S. employee benefit plans, which were not directly related to the audit of the consolidated financial statements. The Audit Committee approved 100% of these Audit-Related Fees pursuant to its pre-approval policy.

Tax Fees. This category includes fees for professional services performed by Deloitte & Touche LLP with respect to tax compliance, tax advice and tax planning. The Audit Committee approved 100% of these Tax Fees pursuant to its pre-approval policy.

Services Provided by Deloitte & Touche LLP

All services rendered by Deloitte & Touche LLP are permissible under applicable laws and regulations, and are pre-approved by the Audit Committee. Pursuant to SEC rules, the fees paid to Deloitte & Touche LLP for services are disclosed in the table above under the categories listed.

Although ratification by stockholders is not required by law, the Audit Committee has determined that it is desirable to seek stockholder ratification of this appointment in light of the critical role played by independent registered public accountants in maintaining the integrity of Company financial controls and reporting. Notwithstanding its selection, the Audit Committee, in its discretion, may appoint new independent registered public accountants at any time during the year if the Audit Committee believes that such a change would be in the best

interest of the Company and its stockholders. If the stockholders do not ratify the appointment of Deloitte & Touche LLP, the Audit Committee may reconsider its selection.

**WE RECOMMEND THAT YOU VOTE FOR THE CONTINUED ENGAGEMENT OF
DELOITTE & TOUCHE LLP AS INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM
TO AUDIT THE BOOKS AND RECORDS OF THE COMPANY FOR
THE FISCAL YEAR ENDING DECEMBER 31, 2008.**

AUDIT COMMITTEE REPORT

The Audit Committee of the Board of Directors is comprised of three directors who are deemed to be independent under New York Stock Exchange listing standards and Securities and Exchange Commission regulations. We operate under a written charter, a copy of which is available on Smith's website, www.smith.com. As required by the charter, we review and reassess the charter annually and recommend any changes to the Board of Directors for approval.

Smith's management is responsible for the preparation and integrity of the financial statements and the independent registered public accounting firm is responsible for auditing those financial statements. The Audit Committee's role under its charter is to provide oversight of management in carrying out their duties and to appoint, compensate, and oversee the work of the independent registered public accounting firm. The Audit Committee is not providing any expert or special assurance as to Smith's financial statements or any professional certification as to the independent registered public accounting firm's work.

In this context, we report as follows:

We have reviewed and discussed with senior management the audited financial statements included in the Company's Annual Report on Form 10-K. Management has confirmed to us that such financial statements have been prepared in conformity with generally accepted accounting principles.

We have discussed with Deloitte & Touche LLP, Smith's independent registered public accounting firm, the matters required to be discussed by Statement on Auditing Standards No. 61, as amended, *Communications with Audit Committees*. This Statement requires independent auditors to communicate certain matters related to the conduct of an audit to those who have responsibility for oversight of the financial reporting process, specifically the Audit Committee.

We have received and reviewed the written disclosures and the letter from the independent registered public accounting firm required by Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees*, with respect to any relationships between the Firm and the Company. Deloitte & Touche LLP has discussed its independence with us, and has confirmed in such letter that, in its professional judgment, it is independent of the Company within the meaning of the federal securities laws.

Based on the foregoing, we recommended to the Board of Directors that the audited financial statements referred to above be included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2007 filed with the Securities and Exchange Commission.

Dod A. Fraser, *Chairman*
Robert Kelley
John Yearwood

This report of the Audit Committee shall not be deemed soliciting material, or to be filed with the Securities and Exchange Commission or subject to Regulation 14A or 14C or to the liabilities of Section 18 of the Securities Exchange Act of 1934 (the Exchange Act), except to the extent that we specifically request that the information be treated as soliciting material or specifically incorporate it by reference into a document filed under the Securities Act of 1933 (the Securities Act) or the Exchange Act. Further, this report will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act except to the extent that we specifically incorporate this information by reference.

OTHER BUSINESS

The Board of Directors does not intend to present any other business for action at the meeting, and the Company has not been advised of any other business intended to be presented by others.

STOCKHOLDERS PROPOSALS

To be considered for inclusion in the proxy statement for next year's Annual Meeting, stockholder proposals must be submitted to the Company in writing by no later than December 12, 2008. In addition, in order for a stockholder to bring any business before next year's Annual Meeting, notice must be received by the Company in writing by no later than December 12, 2008, in accordance with the Company's Restated Bylaws. If we do not receive notice of your proposal within this time frame, our management will use its discretion to vote all the shares for which we have received proxies as the Board may recommend.